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No. 04-146

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

AEROFLOT-RUSSIAN AIRLINES,

Petitioner,

—v.—

MGM PRODUCTIONS GROUP, INC.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITIONER'S REPLY BRIEF

BRUCE E. YANNETT
CARL MICARELLI
(*Counsel of Record*)
DEBEVOISE & PLIMPTON LLP
919 Third Avenue
New York, New York 10022-3916
(212) 909-6000

Attorneys for Petitioner

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ARGUMENT

I.

THE COURT BELOW DECIDED THE QUESTIONS PRESENTED IN THE PETITION.

Respondent's assertion that the questions presented were not decided below, *see* Brief in Opposition ("Opp.") 5-7, is incorrect. The Court of Appeals held as follows:

> [1] the arbitrators found that since the Agreement provided only for transactions between Russo and Aeroflot, it did not contravene the regulations. We accord great deference to the arbitrator's factual findings and contractual construction. ... [2] Even if ... we did not, it would be, at most, doubtful that the Agreement violated the 1995 ITRs. And, as such, the Agreement cannot be said to violate fundamental public policy. *See Parsons & Whittemore Overseas Co. v. Societé Generale de l'Industrie du Papier (RAKTA)*, 508 F.2d 969, 973-74 (2d Cir. 1974).

Appendix to Petition ("App.") 2a-3a. Thus, there are two alternative bases for the Court of Appeals' holding: (*i*) the court deferred to the arbitrators' conclusion that the Iranian Transactions Regulations ("ITRs"), 31 C.F.R. §§ 560.101-560.901, are not violated as long as a U.S. company does not engage in a transaction directly with an Iranian entity, and (*ii*) the court held that a violation of the Iranian Transactions Regulations, unless clear beyond doubt, does not rise to the level of "fundamental public policy" as articulated in the

Parsons case.[1] These two issues are the questions that the Petition presents. *See* Petition ("Pet."), at i.

II.

THE LEGAL ISSUES PRESENTED IN THE PETITION ARE NOT SPECIFIC TO THE FACTS OF THIS CASE.

For the reasons set forth in the Petition, this case presents important issues that have not been, but should be, resolved by this Court. Contrary to what respondent appears to suggest, *see* Opp. 11, this Court has frequently granted certiorari to review summary orders not designated for publication, particularly where, as here, the decision rests on earlier circuit precedent that has not been reviewed by this Court. *See, e.g., Massaro v. United States*, 538 U.S. 500, 503 (2003). The

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[1] Respondent erroneously states that the Court of Appeals "found that the Agreement *did not violate* U.S. 'sanctions laws,'" Opp. 7 (original emphasis), but elsewhere respondent concedes that that court only implied "that the agreement *likely* did not violate the ITRs," Opp. 6 (emphasis added). The court expressed no definite conclusion on whether the agreement actually violated the 1995 ITRs; however, it did not question that the agreement violated the 1997 ITRs, which make explicit that "facilitating" a foreign national's trade with Iran falls within the scope of the prohibition. *See* 31 C.F.R. §§ 560.206(b), 560.208. Had the court actually made an independent effort to parse through the definitions in the 1995 ITRs, it would have seen that the agreement violated those regulations as well. *See* 31 C.F.R. §§ 560.206, 560.304(b), 560.306(a)(2), (e) (1996 ed.) (barring transactions "relating to" "[g]oods which have entered into Iranian commerce," such as the aircraft leased to Iran, or "relating to" "[s]ervices performed" "in Iran," such as the commercial airline service provided by Iran Air, or "relating to" "services performed" by an "entity owned or controlled" by the Government of Iran, such as Iran Air); *see also Comet Enters. Ltd. v. Air-A-Plane Corp.*, No. 2:95CV926, 1996 U.S. Dist. LEXIS 4393, at *16 (E.D. Va. Feb. 27, 1996) ("obtaining orders from Iran Air" violated 1995 ITRs), *rev'd on other grounds*, 128 F.3d 855 (4th Cir. 1997).

courts below saw the case as controlled by the Second Circuit's prior decision in *Parsons* (*see* App. 3a, 9a-10a, 12a), but *Parsons* is not binding on this Court.

Respondent seizes on the phrase "factual findings and contractual construction" in the Second Circuit's order, App. 2a, Opp. 10-11, to argue that this case turns on a question of fact peculiar to this case. But the questions raised by the Second Circuit's decision and presented by the Petition are not fact-specific in the least: first, whether judges should defer to arbitrators as to questions of law concerning the enforceability of their own award in the U.S. under the public-policy exception and, second, whether enforcement of an award directing payment for services in violation of U.S. trade sanctions laws is "contrary to public policy of [the U.S.]" within the meaning of Article V(2)(b) of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 21 U.S.T. 2517 (the "New York Convention").

Respondent also argues that erroneous arbitral factfinding does not give rise to a public policy defense, Opp. 6-7, but Aeroflot has not contested the arbitrators' findings of fact here or in the courts below. Despite the imprecisely drafted language in the Court of Appeals' summary order, no factual dispute was at issue. The Consultation Agreement, the arbitrators' award, and both parties' briefs in the Court of Appeals were all in agreement that Russo's contractual duties ran only to Aeroflot and that those duties consisted of providing consulting services to Aeroflot for leasing Russian commercial aircraft to Iran Air and other Iranian airlines operating in Iran. *See* App. 21a, 24a, 29a-31a; Appellee's Brief 12-13; Appellant's Reply Brief 1-2. The issues before the District Court and the Court of Appeals were pure questions of law: (*i*) whether the undisputed facts as found by the arbitrators amounted, as a matter of law, to a violation of the

applicable U.S. trade sanctions laws, and (*ii*) if so, whether enforcement of the award would be a violation of U.S. public policy under the New York Convention. On each of these questions of law, the Court of Appeals deferred to the arbitrators. *See* Pet. 5-6, 10; App. 2a. Labeling these legal issues as questions of fact or contractual interpretation does not make them such.

III.

THE DECISION BELOW HAS NO BASIS IN PRECEDENT.

Respondent's argument and the decision below fail to appreciate the difference between (*i*) an assertion that the arbitrators' decision violates fundamental morality and justice and (*ii*) the well-established defense that national courts cannot enforce an award based on a cause of action that itself is repugnant to U.S. public policy. While the first of these two branches of the public-policy doctrine is raised by litigants more often—and therefore receives more mention in the case law—there is no support for respondent's apparent suggestion that the second branch of the doctrine can simply be ignored. Where, as here, the underlying contract as interpreted by the arbitrators is alleged to violate national law, it is long settled that the court asked to enforce the award has a duty to make its own independent determination as to whether enforcement of the contract violates public policy. *See generally* Pet. 6-11 (citing cases).

Neither respondent nor the courts below have taken issue with the proposition that a *cause of action* on a contract that violates the Iranian Transactions Regulations is contrary to public policy.[2] It is also clear that an *arbitral award* on a

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[2] *See National Petrochemical Co. v. M/T Stolt Sheaf*, 930 F.2d 240, 243 (2d Cir. 1991) (so holding); *Comet*, 1996 U.S. Dist. LEXIS 4393, at

(footnote continued)

contract that violates public policy as interpreted by the arbitrators is itself unenforceable as violating public policy. *See* Pet. 7, 8, 11 (citing cases). But respondent has advocated, and the courts below have adopted, the conclusion that international arbitration awards subject to the New York Convention are a unique exception to this settled rule, despite the Convention's clear language incorporating the enforcing country's public policy. *See* Opp. 12-13; Pet. 9-10.

Contrary to what respondent suggests, this exception has no support in this Court's precedents. Petitioner relies on cases decided at the stage of a motion to compel arbitration, Opp. 9-10, 12, but those very cases make clear that the decision to allow arbitration to proceed does not deprive "the national courts of the United States ... [of] the opportunity at the award-enforcement stage to ensure that the legitimate interest in the enforcement of the ... laws has been addressed." *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 520 (1974).[3]

Respondent also cannot rely on those cases' general language regarding international comity to support the suggestion that the rules governing the public policy defense in the domestic context somehow fail to apply in the interna-

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(footnote continued)

*16 (same); *Kashani v. Tsann Kuen China Enter. Co.*, 118 Cal. App. 4th 531, 557, 13 Cal. Rptr. 3d 174, 193 (2004) (same). Respondent alludes to cases that, as an exception to the usual rule, have applied a balancing test when the illegality relates only to a peripheral matter, *see* Opp. 14 n.4; but here, the substance of the parties' contract is illegal in its entirety.

[3] *See also Ledee v. Ceramiche Ragno*, 684 F.2d 184 (1st Cir. 1982) (cited by respondent; arising at pre-arbitration stage); *Belship Nav., Inc. v. Sealift, Inc.*, 1996 A.M.C. 209 (S.D.N.Y. 1995) (same).

tional context. This Court's subsequent cases have made clear that the policy favoring arbitration articulated in *Mitsubishi* and *Scherk* extends with equal vigor to the domestic arbitration context.[4] Respondent effectively concedes that a domestic arbitral award on a contract that violates the ITRs would be unenforceable.

Respondent also asserts that the decision below was based on "well-settled" U.S. law, Opp. 14; but as authority for this proposition, it cites only the Second Circuit Court of Appeals' own prior decision in *Parsons* and two district court cases (including one from that circuit) following *Parsons*. *See* Opp. 14-15. Moreover, contrary to what respondent alleges, Opp. 8, case law from other circuits supports Aeroflot's position that an arbitral award on a contract that violates the ITRs is unenforceable under the public policy defense of the New York Convention. *See Indus. Risk Insurers v. M.A.N. Gutehoffnungshütte GmbH*, 141 F.3d 1434, 1445 (11th Cir. 1998) (public-policy standard articulated by this Court in *domestic* arbitration context "applies with equal

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[4] *Mitsubishi and Scherk* distinguished, in the international context, the now-discredited case of *Wilko v. Swan*, 346 U.S. 427 (1953), which had artificially restricted arbitrability of securities claims. But after this Court limited and then overruled *Wilko* in the domestic context, the distinction that *Mitsubishi* and *Scherk* had drawn between domestic and international arbitration largely vanished. *See Shearson/Am. Express v. McMahon*, 482 U.S. 220, 224, 229-20 (1987) (limiting *Wilko*; applying *Mitsubishi* and *Scherk* in domestic context; rejecting attempt to distinguish *Mitsubishi* as international case); *Rodriguez de Quijas v. Shearson/Am. Express*, 490 U.S. 477 (1989) (overruling *Wilko*); *see also, e.g., Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444, 452 (2003) (following *Mitsubishi* in domestic context without comment on its origin as international case); *Quackenbush v. Allstate Ins. Co.*, 517 U.S. 706, 729 (1996) (same); *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 26, 28-31 (1991) (same).

force in the context of international arbitral awards"); *Ministry of Defense of Islamic Rep. of Iran v. Gould, Inc.*, 969 F.2d 764, 773-74 (9th Cir. 1992) (remanding for determination of whether enforcement of international arbitral award under Convention would violate Iran sanctions). The cases that respondent cites as "expressly endors[ing]" the Second Circuit's analysis, Opp. 8, do not even address the relevant issue.[5] *None* of those cases considered the enforceability in the U.S. of an award under a contract that violates U.S. law—much less trade sanctions laws or other laws enacted to protect the national interest.

Moreover, as Aeroflot has explained, the precedents of other nations that are parties to the New York Convention squarely establish that an award on a contract that violates trade restrictions is unenforceable under the public-policy defense set forth in the Convention. Pet. 13 & n.7. Unable to distinguish these cases, respondent disparages them as "outlying" decisions, Opp. 17, yet fails to cite *even one case from any jurisdiction*, or even one article or treatise,[6] that has reached the contrary conclusion.

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[5] Each of those cases dealt with an attempted public-policy attack on the quality or admissibility of the evidence presented to the arbitrators, *Slaney v. Int'l Amateur Ath. Fed'n*, 244 F.3d 580, 593 (7th Cir. 2001); *Indus. Risk*, 141 F.3d at 1445; or the substantive correctness of the arbitrators' decision not going to the legality of the underlying transaction, *M&C Corp. v. Erwin Behr GmbH & Co.*, 87 F.3d 844, 851 n.2 (6th Cir. 1996); *CBS Corp. v. WAK Orient Power & Light*, 168 F. Supp. 2d 403, 415 (E.D. Pa. 2001); or a party's alleged misconduct in the course of the arbitration, *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara*, 364 F.3d 274, 305-06 (5th Cir. 2004).

[6] Commentators on the Convention have agreed that the public-policy defense to enforcement applies where the award violates measures of embargo, blockade, or boycott imposed by the enforcing country. *See* Pet.

(footnote continued)

Respondent's assertion that *Soleimany v. Soleimany*, [1999] Q.B. 785 (C.A. 1998) (Eng.), has been "strictly limited to its facts" by later cases, Opp. 18, is simply wrong. The cases cited by respondent reaffirmed *Soleimany*'s relevant holding that an arbitral award on an illegal contract is unenforceable under the New York Convention, and only questioned certain dicta in *Soleimany* relating to proof of facts.[7] *Soleimany* remains good law, and courts in England and elsewhere have continued to cite and follow it.[8]

IV.

COURTS MAY NOT SUBSTITUTE THEIR OWN VIEWS OF "MORALITY AND JUSTICE" FOR THE FOREIGN POLICY JUDGMENTS OF THE PRESIDENT AND CONGRESS.

Respondent also derides the enforcement of trade sanctions as "parochialism," Opp. 18, and even suggests that U.S. trade sanctions against Iran are no better than the Muslim states' boycott of Israel, *id.*, and that "[t]here is nothing *inherently* wrong" about U.S. citizens trading with the Nation's declared enemies, Opp. 19 (original emphasis). But

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(footnote continued)
9, 14-15 (citing authorities); *see also* Serge Lazareff, *Mandatory Extraterritorial Application of National Law*, 11 Arb. Int'l 137, 145-46 (1995).

[7] *See Westacre Investments Inc. v. Jugoimport-SPDR Holding Co.*, [2000] 1 Q.B. 288, 302 (C.A. 1999) (Eng.); *Omnium de Traitement et de Valorisation S.A. v. Hilmarton Ltd.*, [1999] 2 Lloyd's Rep. 222, 225 (Q.B.D. Comm'l Ct. 1999) (Eng.).

[8] *See, e.g., Al-Kishtaini v. Shanshal*, [2001] EWCA Civ. 264, ¶ 38 (C.A. 2001) (Eng.) (following *Soleimany* to hold that contract violating U.K. sanctions against Iraq was unenforceable); *Mond v. Berger*, [2004] VSC 45, ¶¶ 104-115 (Vic. Comm'l & Eq. Div. 2004) (Austl.) (following *Soleimany* to hold that arbitral award that violated state law would not be enforceable).

whatever political arguments respondent might make for these views, the courts may not decide that mandatory, explicitly extraterritorial laws and regulations adopted by Congress and the President do not constitute "public policy" because they are thought by some to be "parochial" or to have little moral weight.

As authorized by statute, *see* 50 U.S.C. § 1702(a)(1), the ITRs by their express terms apply to acts by U.S. citizens and companies anywhere in the world. *See* 31 C.F.R. §§ 560.206, 560.314. While this Court has justifiably been reluctant to extend U.S. laws beyond U.S. boundaries in the face of legislative silence on the subject, *see The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 9 (1972) (cited by respondent), such concern to avoid judicial "parochialism" has no basis where, as here, the relevant provision of law has *explicitly* extraterritorial effect, *see EEOC v. Arabian Am. Oil Co.*, 499 U.S. 244, 259 (1991) ("Congress, should it wish to do so," may amend statute to apply outside U.S.). It is not the role of the courts, no matter how good their intentions are, to undercut the Nation's foreign policy in the name of promoting international trade.

There is no room to doubt that the Executive and Legislative branches have treated the ITRs as expressing mandatory public policy of the highest importance. Trade sanctions have been a mainstay of U.S. foreign policy almost since the founding of the Nation. *See United States v. Curtiss-Wright Export Corp.*, 299 U.S. 304, 322-24 & n.2 (1936) (discussing history of U.S. embargo laws from 1794). Violations are punishable by substantial fines and lengthy imprisonment. *See* 50 U.S.C. § 1705; 31 C.F.R. § 560.701. The ban embodied in the ITRs, in particular, "is clothed with the most serious of purposes, and it is couched in the broadest of terms," reflecting "the President's appraisal of the nation's

interest in sanctioning Iran's sponsorship of international terrorism, its frustration of the Middle East peace process, and its pursuit of weapons of mass destruction." *United States v. Ehsan*, 163 F.3d 855, 859 (4th Cir. 1998) (reinstating criminal indictment for violating ITRs). Recently, the President has reaffirmed that "the actions and policies of the Government of Iran continue to pose an unusual and extraordinary threat to the national security, foreign policy, and economy of the United States." Notice, *Continuation of National Emergency with Respect to Iran*, 69 Fed. Reg. 12,051 (The President, Mar. 11, 2004). In view of these clear policy statements from the Executive and Legislative branches, the conclusion of the court below that it could bypass construing the ITRs—either by deferring to a foreign arbitral panel or by insisting that only the most blatant violations meet the *Parsons* "morality and justice" standard—disregards the principle of separation of powers and undermines the rule of law.

CONCLUSION

For the foregoing reasons and the reasons set forth in the petition, the petition should be granted.

Respectfully submitted,

BRUCE E. YANNETT
CARL MICARELLI
(Counsel of Record)
DEBEVOISE & PLIMPTON LLP
919 Third Avenue
New York, NY 10022-3916
(212) 909-6000

Attorneys for Petitioner

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